

— Opinion

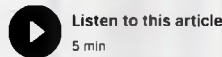
PwC tax leak scandal has exposed partnerships as regulatory havens

The loopholes that allow large accounting firms that look, act and behave much like corporations without being regulated in the same way should now be closed.

Brent Fisse
Lawyer

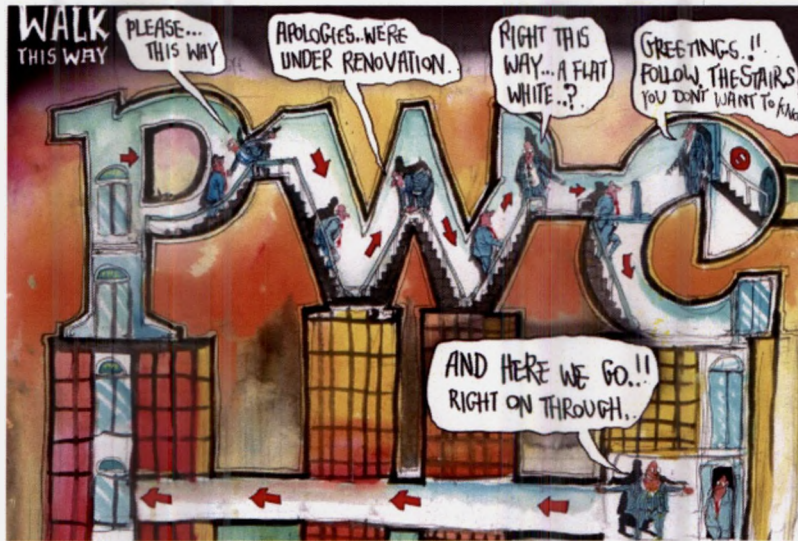


Oct 5, 2023 - 12.37pm



The PwC tax leak scandal [<https://www.afr.com/topic/pwc-tax-scandal-6g22>] has exposed two glaring loopholes in the law where an unincorporated partnership structure is used by large firms.

The first is that the duties of directors and officers under the Corporations Act do not apply, a gap plain from the recent report by former Telstra chief executive Ziggy Switkowski [<https://www.afr.com/companies/professional-services/how-pwc-failed-to-identify-or-deal-with-tax-leaks-scandal-20230928-p5e87u>] into governance issues at PwC Australia.



Large accounting firms look, act and behave much like corporations of comparable size. But there are significant differences. David Rowe

The second is to avoid corporate criminal liability and civil penalty liability for unlawful conduct, including offences under the Commonwealth Criminal Code and breaches of the Competition and Consumer Act and Privacy Act.

These loopholes should be closed. They can be closed by amending the Corporations Regulations to limit the maximum number of partners in an unincorporated partnership to 100.

Large accounting firms typically are unincorporated partnerships. Some have many hundreds of partners. For example, PwC Australia is a partnership under the ACT Partnership Act. It had more than 900 partners at the beginning of 2023. The Corporations Act says that a partnership cannot have more than 20 partners, unless the partnership is incorporated or formed under an Australian law.

However, the Corporations Act enables regulations to set a higher limit for particular kinds of partnership. Regulation 2A.1.01 of the Corporations Regulations allows accounting partnerships to have a maximum of 1000 partners, and law firms a maximum of 400 partners.

These exemptions create havens from corporate regulation.

The governance requirements of the Corporations Act do not apply to unincorporated partnerships. Large accounting firms look, act and behave much like corporations of comparable size. However, directors' duties under the Corporations Act do not apply to unincorporated partnerships. They include the duty to exercise reasonable care and diligence, and the duty not to improperly use information to gain an advantage.

Hinders enforcement

Unincorporated partnerships are also not subject to corporate criminal or civil penalty liability. Commonwealth, state and territorial legislation depends heavily on corporate liability, but partnerships escape corporate liability. This hinders enforcement of a wide range of legislation, including the Corporations Act, the Commonwealth Criminal Code, the Competition and Consumer Act, and the Australian Consumer Law.

The Switkowski report found an "accumulation of poor practices, which went unexamined and uncorrected for many years". However, the issues not covered include possible breaches of directors' duties under the Corporations Act – those duties did not apply to directors or managers of the PwC Australia partnership.

For the same reason, there could not be an independent investigation by ASIC into the conduct of those at the helm of the firm. This is a stark example of a major enforcement gap in the law. It is a haven from corporate regulation.

But closing that loophole is most unlikely to work effectively unless enforcement agencies can pursue corporate as well as individual liability. Letting partnerships avoid liability because they are not incorporated entities is another haven from corporate regulation.

Assume that an accounting firm, Partnership C, engages in cartel conduct with a competing accounting firm, Partnership D, by fixing the lowest prices they will charge for various services to governments.

Partnership C and Partnership D are not subject to corporate criminal liability or corporate liability to civil penalties under the Competition and Consumer Act – the cartel prohibitions apply to a "corporation", not a partnership. If C and D were corporations, the cartel conduct in which they engaged would subject them to corporate liability. The maximum fines or civil monetary penalties for a corporation are the greatest of:

- ◆ \$50,000,000;
- ◆ three times the value of the "reasonably attributable" benefit obtained from the conduct, if the court can determine this; or if a court cannot determine the benefit; and
- ◆ 30 per cent of adjusted turnover during the breach period.

If liability can be imposed only on a partner as an individual, the maximum penalty is \$2.5 million.

Amending the Corporations Regulations to limit the maximum number of partners in unincorporated partnership to 100 would require accounting partnerships to comply with the new limit. Typically, large partnerships would

restructure themselves as corporations. Alternatively, they could restructure themselves as incorporated partnerships.

Under the change proposed, the duties of directors and officers under the Corporations Act would apply to large accounting firms (and large law firms). That would close the first loophole. The new companies or incorporated partnerships formed to comply with the proposed limit of 100 partners would be subject to corporate liability under Commonwealth, state and territorial legislation. That would close the second loophole.

Brent Fisse is principal of Brent Fisse Lawyers. He was a partner in a major law firm for a decade. He co-authored Australian Cartel Regulation (with Caron Beaton-Wells) and Corporations, Crime and Accountability (with John Braithwaite). A recent paper, Accountability and the PwC Tax Leak Scandal, in the Australian Business Law Review sets out 10 accountability concerns about the scandal.

**RELATED****The who, why and what of the PwC tax leak scandal**

<https://www.afr.com/companies/professional-services/the-who-why-and-what-of-the-pwc-tax-leak-scandal-20230926-p5e7nk>

**RELATED****PwC seeks absolution but can it really change?**

<https://www.afr.com/companies/professional-services/pwc-seeks-absolution-but-can-it-really-change-20230929-p5e8ib>

Brent Fisse is Principal of Brent Fisse Lawyers.